Iowa Insurance Division Memo

To: Commissioner Susan Voss
From: Klete Geren, ASA, MAAA, Actuary
Date: October 29, 2012
Re: 2013 Assurant Rate Filing (Individual Major Medical Rate Proposal)

The Iowa Insurance Division (IID) received Assurant's individual rate filing on September 10, 2012 via SERFF, a rate and form filing system [website] hosted by the National Association of Insurance Commissioners. All information in the filing is uploaded to SERFF using PDF and Excel/Word documents. Assurant's proposal calls for an average rate increase of 9% to be effective during calendar year 2013. As required by a 2009 Governor's order to the IID, the filing will receive an independent outside review to give the public additional confidence that the proposal is reasonable and justified. Therefore, the filing will undergo an actuarial review within the IID as well as an independent analysis from INS Consultants, Inc. out of Philadelphia. INS has performed dozens of reviews for the Insurance Division since 2007. As of this date, we have not received the independent report from INS.

Before the results of our review are summarized, it might be useful to provide a brief summary of the filing process in Iowa:

1. Insurance carriers are required to request and receive approval from the Iowa Insurance Division before they can change medical insurance premium rates. Beginning in the second quarter of 2010, all major medical and hospital surgical rate filings will receive additional outside review. Also, if a rate increase proposal for 2012 exceeds 5.8%, a public hearing is scheduled. If the rate increase proposal is above 10%, the carrier is required to file certain information with the federal government (CMS).

2. The carrier's actuaries and attorneys submit the rate change proposal to the IID which includes the following information:

   - A general filing description that summarizes the request, i.e., x% increase proposed, a description of the policy forms affected, and the proposed effective date

   - An actuarial memorandum – this document describes the methodology and assumptions used to determine the amount of the rate increase, i.e., medical inflation, lapse rates, increases in the frequency and severity of claims, higher than expected loss ratios, and other relevant factors. The memorandum also demonstrates compliance with loss ratio standards under the law. Loss ratio means the ratio of claims to premiums.

   - The experience of the policy forms subject to the rate change proposal, i.e., loss ratios of the policy forms to which the rate increase applies.

   - An actuarial certification signed and dated by a qualified actuary

3. The Division's actuarial staff (and its consultants) then independently analyze the carrier's claims experience (loss ratios), claim trends, rate increase history, and other assumptions to determine if the rate increase proposal is actuarially justified.

4. If the Division's staff and its consultants cannot confirm the carrier proposal, a lower (or no increase) could be proposed. This is normally accomplished via email exchanges, face-to-face meetings at the Division's offices, and/or conference calls with the company actuaries.

Other things to consider:

- The Division does not regulate rate changes due to age (getting a year older). The rate at which premium increase due to advancing age is contractually bound based upon the *initial product/policy filing* with the Division.
- The Division does not regulate geographical area factors, nor are there any restrictions on the use of such factors in the code. The factors simply account for differences in the cost of care from one part of the state to another.
- The Division does not regulate smoker and non-smoker differentials.
- The Division does not regulate the difference in premiums between males and females. The relative cost differential is contractually bound in the same fashion that age is.
- The Division does not regulate the difference in premiums between individual contracts vs. family contracts.

While the Division does not regulate the items referenced above, carriers cannot arbitrarily change them. As a practical matter, once the initial policy form (and the initial rates) is submitted to the Division for approval – all of the factors will remain the same throughout the life of the policy form series. In other words, the carrier is not free to change the smoker factor for example. All of the factors such as age, gender, geography, smoker, etc. – which form the basis of a final rate are essentially set in stone from the moment the initial product/policy filing is approved by the Division. Carriers are required to submit new product filings (and rates) with the Division before they can be sold on the market.

Due to the passage of time and the effects of medical inflation, increasing drug costs, and increases in the frequency and intensity of claims – insurance carriers are allowed to increase the premiums to keep pace with these inflationary trends. The goal of the IID's review and external review by the Division's consultants is to ensure that the increase is justified and that the proposed rates will satisfy state and federal loss ratio standards. The company and regulatory process is similar in that both parties try to estimate the rate at which claims are increasing. The rate at which claims are increasing can be calculated by measuring the changes or fluctuations in the loss ratios and/or claims costs. The final process involves setting the premium level so that the target or statutory loss ratio requirement can be satisfied.

The table below summarizes the proposal, i.e., the rate increase by block, the number of policies affected, and the effective date:

Assurant Block	Proposal	# of Iowa lives	Effective Date
John Alden	9%	501	1-1-13
Time Ins. Co.	9%	5,316	1-1-13

For the Division's review, we employed our regular analysis by examining the loss ratios, trends in claims costs, along with setting reasonable target loss ratios. For the combined Assurant block of policies, we set the target loss ratio at 80% which matches the federal Patient Protection and Affordable Care Act (PPACA) standard.

Combined Assurant Block (Time/John Alden)

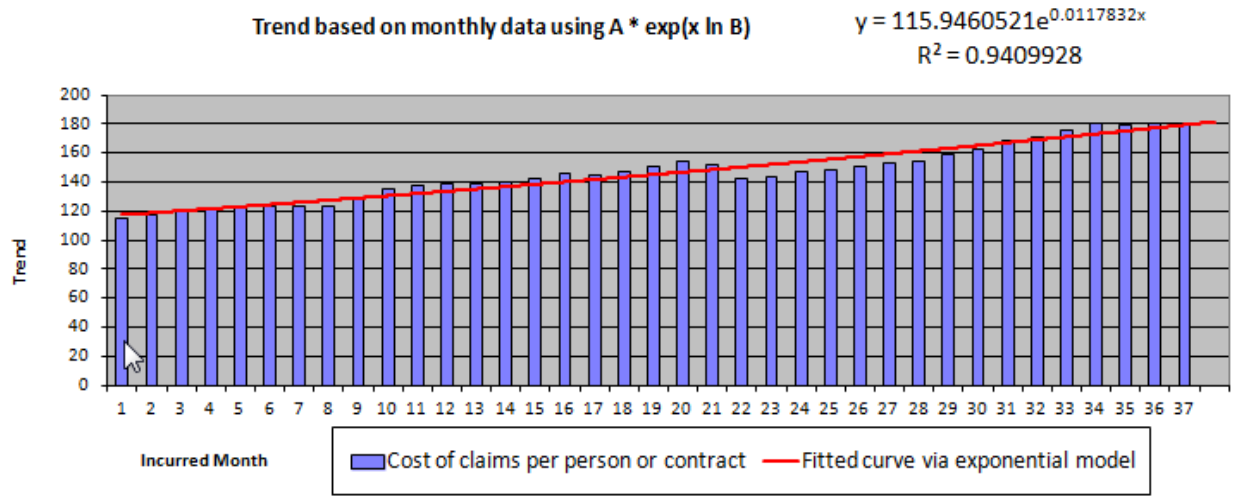
The carrier proposal is 9% to be effective on 1-1-13. Below is a summary of the most recent experience:

Calendar Year	Iowa Earned Premiums	Iowa Incurred Claims	Iowa Loss Ratio
2005	29,778,101	17,909,757	60.1%
2006	30,508,512	21,620,072	70.9%
2007	30,437,037	22,515,627	74.0%
2008	27,938,820	21,208,963	75.9%
2009	25,175,195	21,054,339	83.6%
2010	23,564,235	18,634,048	79.1%
2011	20,777,625	17,069,830	82.2%

As you can see from the table above, the calendar year loss ratios are converging to 80% based upon the last four years of data. These figures meet or exceed the following guides:

- The current 2012 Iowa standard of 75% (per an adjustment permitted by CMS)
- The ultimate federal PPACA standard of 80%, and the Division's target loss ratio of 80%

*Excerpt from the Assurant trend analysis:



*Based on 12 month rolling average claims cost, i.e., sum of monthly incurred claims / member months exposed

Based on this particular method of trend testing, the cost of claims appear to be increasing at a significant rate of more than 15% per year. Using methods other than rolling incremental claims cost suggests an even higher trend rate. This 'other' method involves re-casting the earned premiums as if the current rate schedule been in effect since the beginning. We can then examine the change in the restated loss ratios to estimate the underlying inflationary insurance trend rate. Both of our methods point to an extremely high trend rate for the block of business.

Recommendation based upon the IID review

The Division employs a number of advanced techniques to determine if the proposal is actuarially justified. We calculate a range of rate increase indicators using an internally developed template which relies on the target loss ratio, various lengths of experience periods, prior rate increase history (so that the earned premiums can be restated to a common rate basis), claim costs (including point-to-point incremental changes in the costs), and reported calendar year loss ratios.

Below is a summary of our findings:

	Carrier Proposal	Insurance Division	2013 Legal Requirement
Target loss ratio:	77%	80%	80%
* Trend rate assumption	15.7%	**>15%	NA

The carrier proposal of 77% for 2013 may comply with CMS requirements under current rules, since adjustments are permitted for certain fees and taxes for purposes of federal rebates.

* Growth in cost of claims
** The Division's trend testing template converged on a trend rate of more than 15%, however, for purposes of the actual review process, we used a more reasonable 9.9% figure.

Using our normal method of review to determine the reasonableness of the request, my recommendation is to approve the rate increase. The rate increase indicators generated by the Division's model are higher than the company proposal of 9%. The Division's template assumed an 80% PPACA loss ratio and a 9.9% trend rate which generated a range of increases greater than 9%. The 80% figure is compliant with PPACA standards, and the 9.9% trend rate utilized in our projection is actually less than the 15% indicated trend. Consequently, the carrier's proposal of 9% appears to be actuarially justified and reasonable.

Please note there is an additional layer of protection (beyond regulatory review) provided for under PPACA. If all parties are wrong about this rate increase proposal (the Division's review, the consultant's review, and the company's review), the carrier will be forced to pay rebates to policyholders using a retrospective formula under federal law. Given the experience submitted, I see little to no chance of a rebate when a 75% federal loss ratio standard is in effect (in Iowa) for calendar year 2012.

One final item of note that should be mentioned is that our model is very sensitive to the trend rate and target loss ratio assumptions. Once reasonable target loss ratios are selected with PPACA compliance in mind, the next important step involves the trend rate assumption (growth in cost of claims) to be utilized in the projection of the loss ratios. Selecting a trend factor involves examining the stream of claim costs and/or adjusted loss ratios, where such examination might include calculating year-over-year ratios, changes in the incremental twelve month rolling averages, compound growth calculations, and exponential regression on the natural logarithms of the values being tested. The selection of the trend rate is also complicated by the question of how many months of data should be utilized. For example, examining the last 24 months of claims costs could yield a different trend rate than utilizing the last 48 months. Actuarial judgment is used in the final selection, but in the end – our analysis yielded trend rates and rate increase indicators that were at least as high as the company proposal.

Please let me know if you need anything clarified.

Sincerely,

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